SUPREME COURT, U. S.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1967

No. 361

CLIFFORD L. LIONBERGER,
d.b.a.
Lionberger's Auto Parts,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

REPLY TO RESPONDENT'S MEMORANDUM IN OPPOSITION

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Respondent fails to find judicial authority to offset the relevant decisions of this and other courts that support petitioner's arguments. Nor has respondent the aid of judicial authority to support the three dubious propositions it raises in its answer. Petitioner submits the opposition thus reflects a cause emaciated by a total want of equity.

Petitioner presented three questions for review by this court, to wit:

1. Whether tax discrimination, if gross enough, is equivalent to confiscation and thus subject under the Fifth Amendment to challenge and annulment.

2. Whether the tax on the petitioner operated with so much injustice as to be grossly discriminatory.

3. Whether the tax as collected by the Director of Internal Revenue under color of Section 3440 of the Internal Revenue Code of 1939 followed from a reasonable administrative interpretation of the statute.

Respondent, by avoiding the first two questions, seeks to defend its action in collecting a discriminatory tax solely by reference to the third. Apparently, respondent concedes that the tax on petitioner operated with so much injustice as to be grossly discriminatory and was thus equivalent to confiscation. If so, then the tax as collected is subject to challenge and annulment even if the Internal Revenue Service's action may have followed from a reasonable administrative interpretation of the statute.

Petitioner, nevertheless, finds respondent's propositions in support of its interpretation of the statute so lacking in merit that he elects to make this reply, though under the circumstances it might be deemed unnecessary.

Respondent first proposes that Section 3403(b) of the Internal Revenue Code of 1939 "imposed an excise tax on a manufacturer's 'sale(s)' of trailers," (Oppos. 1). But, careful reference to Section 3403 does not support respondent's first proposition. The opening (and controlling) clause of Section 3403 is the sole clause imposing a tax in the whole of Chapter 29 of the Internal Revenue Code and it is unambiguous:

> *There shall be imposed upon the following articles* sold by the manufacturer, producer, or importer, a tax equivalent to the following percentages of the price for which so sold: (emphasis added by petitioner.)

Petitioner submits again (see Petition, 13) that Congress imposed the excise tax *on* certain *articles* of manufacture,

not on transactions by manufacturers. The transaction is only the *taxable event* which imposes the tax *on the article.* The tax on articles subject to the tax was to be computed upon the basis of the price for which articles were sold. Chapter 29 (Sections 3441, 3444, Pet. 5, 6) provided that the price for which sold represented the *price* fairly obtainable by manufacturers selling in arm's length transactions in the ordinary course of trade (i.e., the fair market price). Congress explicitly provided so in Sections 3441 and 3444 wherein "sale price" is carefully defined. Section 3441(a) specifies that the manufacturer's sales price is to be determined at the point of shipment f.o.b. Section 3441(b) specifies that where sales are made (1) at retail, (2) on consignment, or (3) because of untypical conditions at less than the fair market price, the tax is to be computed on the price for which such articles are sold in the ordinary course of trade by manufacturers.

Petitioner notes that respondent makes no reference to Section 3441. The reason for such reticence is clear. The very existence of Section 3441 cuts the ground out from under respondent's opening proposition, to the effect that the tax is on sales as such. The second proposition hinges upon the first.

Respondent's second proposition (which was adopted by the court below) is that Section 3440 of the Code "taxed each of petitioner's leases of each trailer he manufactured" (Oppos. 2). Reference to Section 3440, (Pet. 4, 5) even without reference to other sections of Chapter 29, lends no support to the proposition. Section 3440 does not provide for a tax upon 'leases'; it merely provides that "the" lease of an article (by the manufacturer) shall be considered a taxable sale of such article. Obviously, if the lease by a manufacturer of a taxable article is to be considered a sale of the article, Section 3441 should apply to define the manufacturer's 'sale price' of such article. Section 3441(c) specifically applies to leases. Obviously Section 3441(a) and (b) must also apply.

The trial commissioner found:

> . . . purely as a matter of fact, the first use to which the trailers involved in this suit were put after their manufacture was in the retail end of plaintiff's business, and in point of time preceded the use or uses to which the trailers were subsequently put by customers who hired them to haul their personal effects. (Finding of Fact No. 4, Pet. 39, 40.)

Clearly, on the basis of this finding, Section 3441(a) limits the tax to the f.o.b. sale price of the trailer at the time petitioner "shipped" it to one of his rental lots. Petitioner's trailers were marked with his name and that of Nationwide, they were licensed in petitioner's name, and they were stored at his several rental locations and held out for rental (Finding No. 4, Pet. 39). Such constituted a use of the trailers by the manufacturer thereof, and the provisions of Section 3444 ought have applied. However, petitioner submits that whether his trailers were rendered taxable on the basis of a lease/sale (Section 3440) or a use/sale (Section 3444) is of no ultimate consequence because the correct sale price for tax purposes would be the same in either event, *i.e.*, the fair market price.

Even if it is assumed that the lease to the ultimate customer constituted the taxable event, the trial commissioner found that the average rental fees of petitioner's trailers were for small sums ($10 to $25), substantially less than the $214 fair market value of the trailers (Findings No. 9, 18; Pet. 42, 45). Accordingly, Section 3441(b)(3) was applicable to determine the correct sale price for tax purposes. Findings of Fact No. 6, 7, 8 and 9 (Pet. 40, 41) show that the "majority of the trailers manufactured by petitioner and involved in this suit were rented through a succession of consignments to other Nationwide members." Hence, Section 3441(b)(2) was applicable to determine the sale price of the trailers. Finding No. 1 (Pet. 37) indicates that petitioner's trailers were designed for towing behind *passenger* automobiles. Finding No. 2 (Pet. 38) indicates that the

gross rentals on an average trailer over its 10 year useful life would exceed by approximately 18-plus times its sale value when new. Finding No. 4 (Pet. 39) indicates that the trailers were rented by '*users.*' These and other findings of fact clearly show the retail nature of petitioner's trailer rental business and demonstrate conclusively that Section 3441(b)(1), too, was applicable to determine the correct 'sale price' for excise tax purposes.

Respondent's third proposition is that because Congress amended the Internal Revenue Code in 1958, it moots the issue for taxable years after 1958 and thus, "there is no warrant for review in this court" (Oppos. 3). This astounding hypothesis rests on the absurd premise that because an unlawful evil has been finally stopped, the harm previously done is automatically assuaged. Respondent's proposition also ignores the fact that petitioner's claim covers years prior to 1958. Further, even though Congress' subsequent clarification in 1958 of the scope and purpose of the manufacturer's excise tax may prevent future administrative misinterpretation of the same point, Congressional clarification does not resolve the constitutional issues raised by petitioner, nor does it provide relief for the harm done, the very existence of which subsequently induced Congress to clarify the language of the statute.

It would be sheer negligence for appellant's attorneys to fail to point out to this honorable court the total inappropriateness of respondent's third proposition. It is so deficient in merit that if it were adopted by this court (which serves as the fountainhead and ultimate repository of equity in the United States), it would tend to induce this court to deny any remedy to a citizen severely and inexcusably discriminated against because of administrative blunder. Such a ruling would also deny the most fundamental right of all, the right to equal justice under the law. This is unquestionably so where a confiscation of property ensues contrary to statute, contrary to Congressional policy, and in complete disregard of any meaningful interpretation of constitutional due process.

Respondent asserts that Congress clearly intended "that *such* lease by a manufacturer of a taxable article 'including . . . any subsequent lease' was to be taxed as a sale" (Oppos. 3). Here, respondent feigns to rely upon the parenthetical clause in Section 3440. But, in fact reliance is placed upon the substitution of respondent's own words "*each* lease" for the words in the statute, viz., "*the* lease" (note the singular).

Petitioner submits that respondent ought not be so confused by the purpose for the parenthetical clause. In his brief to the court below, respondent (there the defendant) in speaking of the parenthetical clause, adduced that Congress inserted it in 1941 "apparently in response to the fact that many business machines were being leased *rather than sold* and in response to some *possible* confusion respecting the scope of Section 3440 with respect to *these* leases" (Def.'s Brief, September 9, 1966, p. 14, emphasis added by petitioner.)

Petitioner submits that the only possible confusion which could arise with respect to the scope of Section 3440 as originally worded was the extent to which Section 3441(c) (which provided for installment payments against the tax in the case of certain classes of transactions), might limit the collection of the full 'sale price' of leased articles in the event *the first lease* were to terminate before the taxable price could be fully reached by the tax. This theoretical problem might have arisen because only *new* articles were subject to the tax. A subsequent lease might conceivably have been held to be a sale of a *used* article. But, the notion that Congress intended, through the parenthetical clause, to impose an income tax on gross rentals from all leases of taxable articles (throughout the life of the article) is inherently incredible.

Respondent references *McClintock v. Westover*, 167 F.2d 601 (Oppos. 3). In *McClintock*, the taxpayer was engaged in the business of manufacturing and supplying decorative rubber trimmings, resembling parsley, to meat markets. The taxpayer entered into so-called "rental agreements" with its

customers, under which it agreed to replace fifty per cent of the "parsley" every 60 days. In the light of this arrangement, it is reasonable to assume that the useful life of the "parsley" was approximately two or three months. It is noted that the sample "rental agreement," set out in a footnote to the decision, ran for a period of three months. The court's decision that the excise tax was properly imposed on the so-called rental receipts, and that these constituted the sale price, is supportable on those facts. The taxpayer's tenuous claim that *he used* the "parsley" *in his business* was pardonably scoffed at by the court.

The taxpayer in *McClintock* always leased his product for its useful life to a single lessee, and never sold his product. There is no evidence to show that if McClintock had competitors that they operated differently than he did. Clearly, where manufacturers generally lease some articles and never sell them (as for example, some business machines, bus tires, rubber parsley), competitive inequalities do *not* exist to a degree sufficient to warrant the administrative duty imposed by Sections 3441 and 3444 of determining a tax base on new articles where no sales at the market price were made. Petitioner both rented and sold trailers *of his own manufacture.* (Finding of Fact No. 1, Pet. 37). The fair market price was easily determinable and has been stipulated (Finding No. 2a, Pet. 37). Petitioner's trailer rental business was easily severable from that of trailer manufacture (Finding No. 3b, Pet. 39). Petitioner's rentals were for short periods of time to numerous different customers (Finding No. 5, Pet. 40). Competition was intense (Finding No. 20, Pet. 46). None of the conditions that supported the *McClintock* decision pertain to petitioner. *McClintock* is an entirely different factual situation.

Respondent correctly points out that Congress intended a manufacturer to pass the tax on by adding the tax to the sale price. Respondent asserts that petitioner failed to pass on the tax because of two decisions he made; (1) not to

pay any tax, and (2) not to use separate corporate entities for his manufacturing and rental enterprises (Oppos. 4). Finding No. 3 (Pet. 39) indicates that the manufacture of trailers by petitioner was a relatively simple operation requiring no special plant facilities or heavy machinery and only a nominal investment. In essence, all petitioner did was assemble a wooden, tarp-covered box and afix it between two wheels mounted on an axle. Petitioner purchased all the component parts and assembled trailers in his garage. Petitioner never attempted to avoid paying the manufacturer's excise tax; he just never thought of himself as a manufacturer. When the tax was assessed, petioner paid it. Whether or not petitioner consciously attempted to pass on the tax in the 'sale price' is immaterial. An excise tax based upon the market price cannot fail to be passed-on in the price of taxable articles when competitive conditions exist in an industry. This is because such articles necessarily are priced by the market, regardless of whether a profit is made by any particular manufacturer. This is axiomatic. It is equally impossible for a taxpayer to pass on a discriminatory tax to the full extent that the tax is discriminatory. In the science of economics, it is axiomatic that all else being equal one engaged in a competitive business must either price his product competitively or else he must witness an ebbing away of his sales as his customers are drawn to his competitor's more cheaply priced product.

It is also axiomatic that if one prices his product competitively, (as a responsible businessman must), then all else being equal, his profits will be those generally prevalent in his type of business. However, if all things are not equal because one business carries a higher tax burden than its competitors, then the profit realized by the business bearing the greater burden will be relatively less (to the full extent of the greater burden of the tax) than it would have been had the tax burden been equal. Clearly, petitioner could not have passed on the tax to the full extent that it exceeded the tax properly payable on the 'sale price' of his trailers.

In his affidavit of November 26, 1963 (Pltf.'s Reply Brief to Deft.'s Cross Motion for Summary Judgment, April 29, 1964, Appendix B, Ct. Claims), petitioner stated:

> That many of said trailer rental businesses competitive to my business did not manufacture automobile utility trailers and in fact on several occasions said businesses purchased automobile utility trailers from my business which did manufacture them.

Petitioner's competitors who purchased trailers from him had only to pass on the tax on the one-time sale price. But, when petitioner 'sold' one of his trailers to himself, he had to try to pass on, not an excise tax on the market price of the trailer, but an income tax on the gross life time rental fees of the trailer, approximately half of which rental fees did not even constitute business income to petitioner. While an excise tax can be fully passed on to another, an income tax cannot. Any attempt to pass on an income tax generates additional income in turn subject to the tax.

Respondent affirms that petitioner could have escaped the unending excise tax on 'leases' if he had used distinct corporate entities for his separable manufacturing and leasing business (Oppos., 4). Petitioner is astounded that respondent suggests this fact as a justification for gross tax discrimination. Congress provided in the statute that a manufacturer must pay a tax to be determined at the time of sale (including the lease-sale and use-sale) of certain articles of manufacture. Nowhere did Congress imply in the statute that a retail merchant who might choose to produce articles incidental to his rental business (or any other taxpayer) *must first set up a separate manufacturing corporation* in order to escape having the manufacturer's excise tax fall upon the gross income from his retail business, and in addition, to enable him to avoid the payment of a manufacturer's excise tax upon a part of the gross income of yet other retail businessmen. The Mad Hatter never perplexed Alice with so amazing a legalism.

Respondent's citation of *Magnano Co. v. Hamilton*, 292 U.S. 40 (Oppos. 4) is also irrelevant. Petitioner does not challenge the act of Congress (Pet. 12). Finally, respondent's reference to the 1958 amendments to the excise tax statute (Oppos. 4, 5) is thoroughly irrelevant. Even if the amendments were significant, an amendment to a law is not persuasive of the intent of a prior Congress many years before; and it does not even support a presumption of that Congress' intent. At most, it is the later Congress' interpretation of existing law and the application thereof. In *United States v. Ryder*, 110 U.S. 729, this court stated: "It will not be inferred that the legislature in revising and consolidating the laws intends to change their policy unless such intention be clearly expressed."

In this regard the late Justice Frankfurter offered wise and respected counsel:

> "We do not delve into the minds of legislators or their draftsmen, or committee members, because. . . in many instances where a problem of meaning arises . . . the enactment was not directed toward the troubling question."[1]

The issue before this court concerns the taxpayer's right to substantive equality in tax treatment. To yield to respondent's dangerous propositions is only to encourage laxity in the exercise of administrative duties. Laws will be administered as laxly as the law permits, and this is an issue of continuing importance.

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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[1] Frankfurter, Felix, "Some Reflections on the Reading of Statutes," *2 Record 213*, Association of the Bar of the City of New York.

CERTIORARI DENIED